

THE OFFICE OF REGULATORY STAFF

DIRECT TESTIMONY

OF

Carey M. Flynt

October 25, 2007



DOCKET NO. 2007-4-G

**Annual Review of Purchased Gas Adjustment and Gas
Purchasing Policies
of Piedmont Natural Gas, Inc.**

**DIRECT TESTIMONY OF CAREY M. FLYNT
ON BEHALF OF
THE SOUTH CAROLINA OFFICE OF REGULATORY STAFF
DOCKET NO. 2007-4-G**

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND OCCUPATION.

A. My name is Carey M. Flynt. My business address is 1441 Main Street, Suite 300, Columbia, South Carolina 29201. I am employed by the State of South Carolina as Manager of the Gas Department for the Office of Regulatory Staff (“ORS”).

Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A. I received a Bachelor of Science Degree in Business Administration, with a major in Accounting from the University of South Carolina in Columbia in 1975. I was employed at that time in the electric and gas utility industry and gained twenty five years experience in this field. In October 2004, I began my employment with ORS. I have testified on numerous occasions before the Public Service Commission of South Carolina (“Commission”) in conjunction with natural gas issues.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to address the purchasing policies of Piedmont Natural Gas Company, Inc. (“Piedmont”), including the hedging program, the Gas Cost Recovery Mechanism (“GCRM”) and the Industrial Sales Program (ISP).

Q. WHAT IS THE REVIEW PERIOD FOR THIS PROCEEDING?

A. The review period encompassed the twelve-month period April 1, 2006 through March 31, 2007.

1 **Q. PLEASE DISCUSS PIEDMONT'S PURCHASING PRACTICES.**

2 **A.** Piedmont must meet the demands of its firm customers on a peak day. Piedmont has
3 firm transportation capacity on the Transco, Columbia Gas and East Tennessee
4 Transmission pipelines. The Company has firm contracted supply, storage and
5 peaking LNG quantities to meet its firm obligations. It is very important that the
6 volume of gas needed for that peak day is available for the firm class of customers. It
7 would be imprudent to plan for interruptible supplies to serve the Company's firm
8 customers on a peak day. Natural gas customers, who utilize natural gas for heating
9 their homes, cooking, water heating and other essential needs, expect the natural gas
10 supply to be available. These firm customers have no alternate fuel capability and
11 must have natural gas available 365 days a year.

12 **Q. PLEASE DESCRIBE PIEDMONT'S SUPPLY CAPABILITIES.**

13 **A.** For the 2006-2007 winter period, Piedmont had firm supply contracts capability
14 totaling 1,356,642 dekatherms. This supply included contracts with suppliers and
15 contracted storage service on the Transco and Columbia gas systems. Additionally,
16 Piedmont has its own Liquefied Natural Gas (LNG) facilities available along with its
17 contracted storage to flow additional natural gas into the system when needed and to
18 balance flowing supplies with system load requirements.

19 **Q. WERE PIEDMONT'S CONTRACTED CAPACITY/DEMAND**
20 **ENTITLEMENTS AND ITS PEAKING CAPABILITIES SUFFICIENT TO**
21 **MEET THE REQUIREMENTS OF ITS FIRM CUSTOMERS?**

22 **A.** Yes. For the winter period ending March 31, 2007, Piedmont had firm demand
23 entitlements and peaking capabilities of 1,356,642 dekatherms, as compared to the

1 Design Day demand requirements of 1,314,108 dekatherms. This analysis indicates
2 the Company had adequate firm supplies to meet its firm customer's requirements.
3 ORS recommends that the Company continue to monitor its firm supply capabilities
4 very closely, especially with regard to future growth on the system and the many
5 changes being experienced in the natural gas industry.

6 **Q. DID ORS CONCLUDE THAT THE COMPANY ACTED PRUDENTLY IN**
7 **PURCHASING SUPPLIES AND CONTRACTING FOR CAPACITY TO MEET**
8 **THE REQUIREMENTS OF ITS FIRM CUSTOMERS?**

9 **A.** Yes. The Company uses what they refer to as a "best cost" gas purchasing policy.
10 This policy consists of five main components -- price, security, flexibility,
11 deliverability and supplier relations. These components are all interrelated and
12 weighed on their importance. Piedmont has been very active in purchasing supplies
13 directly on the market and making arrangements through interstate pipelines for the
14 delivery of these supplies. ORS's observations of Piedmont's gas purchasing policies
15 indicate that Piedmont is continuing its attempts to get the best terms available in its
16 negotiations with suppliers. Also, Piedmont has been very active in FERC
17 proceedings.

18 In addition, ORS believes Piedmont has used the spot market to prudently purchase
19 supplies at prices competitive with industrial alternate fuels, as well as reducing costs
20 to high priority customers.

1 **Q. WHAT WAS THE CONCLUSION ORS REACHED AS TO THE REVIEW OF**
2 **PIEDMONT'S HEDGING PROGRAM?**

3 **A.** While the Company failed to provide regular reports to the Commission and ORS on
4 the results of its hedging program during the review period, ORS determined that
5 Piedmont did manage its Hedging Program in a reasonable and prudent manner.

6 **Q. DID ORS REVIEW THE COMPANY'S FORECASTED FUTURE**
7 **REQUIREMENTS AND THE COMPANY'S STEPS TO MEET THIS**
8 **DEMAND?**

9 **A.** Yes. ORS reviewed the Company's forecasted future demand requirements and the
10 activities the Company is taking to insure the reliability of these supplies. Piedmont
11 has taken a number of steps in securing firm supplies for future demand on its system.
12 These steps range from negotiating with pipelines for capacity on the interstate
13 systems to acquiring additional storage capacity to negotiating contracts with
14 suppliers. Exhibit CMF-1 lists Piedmont's Carolina's Storage Capacities and
15 Maximum Daily Withdrawal Quantities (MWDQ).
16 Piedmont has an obligation to maintain adequate supplies at just and reasonable costs
17 to serve its customers. ORS found that the Company is prepared to meet this
18 responsibility.

19 **Q. PLEASE DESCRIBE PIEDMONT'S APPROVED GAS COST RECOVERY**
20 **MECHANISM.**

21 **A.** The purpose or goal of Piedmont's GCRM is to permit the Company to recover the
22 prudently incurred applicable actual cost of gas from its customers. The recovery of
23 this cost consists of a two part cost of gas component consisting of a Demand cost of

1 gas component and a Commodity cost of gas component. The Demand component
2 includes all capacity charges for the transportation and storage of gas which are not
3 billed on the volume of gas actually purchased or transported by the Company. The
4 Commodity cost of gas component is comprised of charges for the volumes of gas
5 purchased. These charges are not associated with the capacity charges for
6 transportation and storage, or in other words, all charges other than Demand Charges.
7 The GCRM provides that Piedmont establish a Benchmark Commodity Cost of Gas
8 which is the Company's estimate or forecast of the City Gate Delivered Cost of Gas
9 for gas supplies, excluding Demand Charges.

10 The GCRM provides for the recording of the monthly differences between the actual
11 cost of gas purchased and the rate billed to the customer into the Company's Deferred
12 Account No. 253.04.

13 ORS has noted further adjustments are required regarding this account which are
14 detailed in the testimony of ORS witness Sullivan.

15 **Q. DOES PIEDMONT'S APPROVED GAS COST RECOVERY MECHANISM**
16 **ALLOW FOR ADJUSTMENTS TO THE BENCHMARK COMMODITY COST**
17 **OF GAS?**

18 **A.** Yes. The Benchmark Commodity Cost of Gas may be adjusted from time to time to
19 recognize the current market price of gas. These requests are filed with the
20 Commission and ORS for approval by this Commission. The GCRM also allows for
21 the same type adjustment for the Demand Cost of Gas Component, although the
22 Demand Component does not change as frequently as the Commodity Cost of Gas
23 Component.

1 **Q. WHAT IS THE CURRENT BENCHMARK COST OF GAS INCLUDED IN**
2 **THE COMPANY'S RATES?**

3 **A.** The current benchmark cost of gas included in the company's rates is \$8.50 per
4 dekatherm which became effective August 1, 2007. ORS does not recommend any
5 change to the benchmark cost of gas at this time.

6 **Q. HOW DO THE COMPANY'S GAS COSTS RECOVERY MECHANISM AND**
7 **INDUSTRIAL SALES PROGRAM COMPARE TO THOSE OF THE OTHER**
8 **GAS UTILITIES UNDER THE COMMISSION'S JURISDICTION?**

9 **A.** Piedmont's GCRM and Industrial Sales Program are somewhat different than the
10 operation for the one other South Carolina's gas utility. The major difference is
11 Piedmont has the opportunity to recover all negotiated losses from its competitive
12 industrial customers. Piedmont utilizes Rate Schedule 208 (Exhibit CMF-2), to
13 provide negotiated sales or transportation service to customers that would otherwise
14 utilize alternate fuels because the maximum published rates may not be competitive at
15 times. Due to the opportunity Piedmont has to recover negotiated losses through the
16 operation of the deferred account, it is imperative that Piedmont negotiate its rate to
17 industrial customers only to the level that is competitive with the alternative fuel prices
18 without going below the Company's actual cost of the gas. Piedmont utilizes its
19 monthly weighted average cost of gas (WACOG) as the basis for negotiations of
20 monthly sales service and will not negotiate a sales price that is lower than the
21 WACOG.

22 **Q. DID ORS FIND THAT THE COMPANY HAS BEEN NEGOTIATING A**
23 **PRICE WITH THE INDUSTRIAL CUSTOMER ONLY TO THE LEVEL**

**WHICH IS COMPETITIVE WITH THE ALTERNATE FUELS AND NOT
BELOW THEM?**

A. Yes. When Piedmont is negotiating its rate to compete with alternate fuels, the Company ensures three objectives are met. These are:

- The quoted rate does not undercut the cost of the alternate fuel;
- The most accurate market prices are utilized for both alternate fuels and natural gas and,
- Negotiating the highest possible margin.

The first step to ensure that Piedmont does not undercut alternate fuel prices is to identify the reasonable range of costs for specific alternate fuels early in the negotiation process. A number of alternate fuel prices are identified by Piedmont's account representatives and entered into an online database. Both Piedmont management and account representatives have real time access to these alternate fuel prices in a format that allows the comparison of prices from various customers and various locations across the service area. The comparison of these customer alternate fuel costs allows Piedmont to identify the range of market prices of various types of fuel and to identify customer submitted alternate fuel prices that do not fall in an expected cost range. Piedmont contacts these customers again and requests verification of alternate fuel prices when the prices supplied by the customer are lower than expected.

Additional resources are available to identify the market pricing for alternate fuels. These resources include various Internet sites such as the Energy Information Administration, NYMEX, Amerada Hess, WTRG Economics, Industrial Fuel, Online Energy, Horizon Energy, and Oil Energy.

1 When Piedmont is negotiating its transportation rate, Piedmont utilizes two sources to
2 understand the market cost of gas provided by a third party marketer. These sources
3 include NYMEX for the commodity cost and internal gas supply personal to identify a
4 reasonable basis cost. If the Company thinks quoted total delivered price for natural
5 gas is excessive, the Company will offer a negotiated price based on what the
6 company thinks is reasonable.

7 It is important to understand that Piedmont's approved negotiating process does not
8 allow the Company to retain all loads each month, but it does allow the Company the
9 opportunity to provide natural gas sales and transportation service to avoid lost sales in
10 the market place.

11 **Q. DOES ORS HAVE ANY RECOMMENDATIONS ADDRESSING REPORTING**
12 **REQUIREMENTS OF PIEDMONT?**

13 **A.** Yes. ORS would remind Piedmont of the language in Commission Order No. 88-294
14 addressing reporting requirements. Order No. 88-294, dated April 6, 1988 at page 3,
15 item number 4 states, "The Company is to maintain an account reflecting its gas costs
16 each month, the amount of gas costs recovered each month, and amounts deferred
17 from month to month. The company is to file with the Commission a report on a
18 monthly basis showing the status of the account." The last report received was for the
19 month of June, 2006. ORS recommends that the Company begin filing these reports
20 on a monthly basis with the Commission and the ORS beginning with the report for
21 the month of November 2007.

22 Additionally, regarding Hedging Reports, the Commission in its Order No. 2002-223
23 in Docket No. 2001-410-G, dated March 26, 2002 at page 7 states, "Fifth, under the

1 plan, Piedmont will provide regular reports on the status of the program and the results
2 of its hedging program and the results of its hedging activities such that the
3 Commission or any other interested party may seek modification or termination of the
4 plan on a prospective basis.” The last report received was for Quarter ending June
5 2006. ORS recommends the Company be required to begin filing these reports on a
6 monthly basis with the Commission and the ORS beginning with the report for the
7 month of November 2007.

8 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

9 **A.** Yes, it does.

Piedmont Natural Gas Company, Inc.

**Carolina's Storage Capacity
4/1/2006 - 3/31/2007**

Pipeline	Rate Schedule	Storage Capacity (Dts)	MDWQ (Dt)
Transco	GSS	4,293,463	77,475
Transco	WSS	9,126,563	107,373
Transco	ESS	750,337	74,576
Transco	ESS	1,132,997	113,764
Transco	SS	100,000	10,000
Pine Needle	LNG-1	2,634,000	263,400
Dominion	GSS	799,800	13,330
Columbia Gas	FSS	5,137,358	86,368
PNG - Duncan (West)	LNG-SS	1,035,000	100,000
PNG - Barragan (East)	LNG-SS	1,035,000	88,000

Piedmont Natural Gas Company, Inc.

P.S.C.S.C. Tariff

RATE SCHEDULE 208
NEGOTIATED SERVICE

Applicability and Character of Service

On occasions, the Company may have gas that it cannot sell or transportation service that it cannot provide pursuant to its rate schedules because its maximum rates are not competitive with alternate fuels or energy sources. On such occasions, a service opportunity is lost to the Company and to its Customers. This Rate Schedule is designed to permit the Company to provide services at negotiated rates.

Gas service under this Rate Schedule is available on a limited term basis to all non-residential Customers in the area served by the Company in the State of South Carolina who receive services under the Company's Rate Schedules 202, 232, 252, 262, 242, 203, 213, 204 or 214. The Company may provide negotiated transportation and sales service to Customers who receive service under Rate Schedule 214 in order to compete with alternate fuels or energy sources. Unless otherwise agreed to by the Company, service under this Rate Schedule is interruptible and the Company has the right to discontinue such service on one hour's notice.

Rate

The rate to be charged for gas service pursuant to this Rate Schedule is subject to negotiation between the Customer and the Company.

Payment of Bills

Bills are net and due upon receipt. Bills become past due 15 days after bill date.

Late Payment Charge

A late payment charge of one and a half percent (1 ½%) per month will be applied to all balances not paid prior to the next month's billing date.

Service Interruption and Curtailment

Gas service under this Rate Schedule is subject to the provisions contained within Rate Schedule 206, "Schedule for Limiting and Curtailing Service".

Applicable Documents Defining Obligations of the Company and Its Customers

Service under this rate schedule is subject to the Rules and Regulations of the Public Service Commission of South Carolina ("Commission Rules") and to the Company's Service Regulations. Among other things, the Commission Rules and the Company's Service Regulations permit the interruption or curtailment of service under certain conditions, including events of *force majeure* and operating conditions. A copy of the Commission's Rules may be obtained from the Public Service Commission of South Carolina, 101 Executive Center Dr., Columbia, SC 29210, upon payment of the applicable fee. The Company's Service Regulations may be obtained at each of the district offices of the Company. Unofficial copies of the Company's Service Regulations are available at the Company's Web Site at www.piedmontng.com.